ROYDS REPORT

January 2023

Market Volatility – Normal but not Fun, Sometimes Profitable

According to Wikipedia, 2 of the 10 biggest single day market gains (on the S&P 500 index) since 1923 happened in Mar 2020, and 2 of the 10 worst single day drops since 1923 were also in Mar of 2020. (Another 2 of the 10 biggest gains and 2 of the 10 biggest losses occurred in 2008 during the Great Financial Crisis. So many of our clients have endured those too.) So, no wonder investors felt quite bruised at the start of Covid. Luckily it didn't take too long to recover from the 2020 drops. And anyone brave enough to add money to the market after those drops had a chance to participate in quick gains as the market rebounded.

We only remember a few times before 2020 when, if the market was strongly up before lunch, it ended dramatically down by the close of the market at 4 p.m. That sure hasn't been true this year. Since computerized trading and day trading became prevalent this century, and with the added fears of Covid, inflation and the Ukraine Invasion, intraday market swings seem to have gotten worse. Huge day to day market changes seem to have become more common too.

How does this affect us? On days when we see particularly strong volatility, if someone is selling one fund to buy another, we sometimes recommend not waiting till the next day to buy the new fund (because you don't know the sale proceeds until the next day). Buying the day after a sale has always been the normal practice. Instead, we use about 95% of the expected sale proceeds to buy the new fund on the same day as the sale of the old fund, and we buy more of the new fund the next day with any excess proceeds. It cuts the risk of selling on a low market day and buying when the market is much higher/more expensive the next day. (It also eliminates the chance that the market might be cheaper to buy into the next day. Instead, one is selling and doing most of the buying under the same market conditions. Most people would rather eliminate the risk of buying high than trying to time the market to perhaps buy on a bargain day.) This strategy wasn't necessary in the past, because day to day changes were pretty small.

The fact that single day market gains of over 5% (up to a record 11.4% one day gain) sometimes occur is one of the reasons why people should never sell when the market is down, thinking that they'll get back in the market later, when things seem less scary. If someone is out of the market, sitting in cash, on the day when a big 5% plus gain happens, they could miss a huge part of the recovery's gains. If they miss a few of these high up-market days before getting back into the market, it could take years longer for their account to fully recover. We can't predict when these big market gains will occur; no one can. That's why we stay invested even when we hear there could be more bad news coming. This last quarter is a case in point. Throughout the last half of 2022, there was increasing talk of a recession coming in 2023. Despite that, the market was up in October and November. It fell back in December, but that drop didn't wipe out the gains of October and November. It's a good thing we didn't bail out of the market in September and end up missing the October and November gains. The way to get the long-term returns that equity markets offer is to stay continuously invested for the long-term.

Source: https://en.wikipedia.org/wiki/List_of_largest_daily_changes_in_the_S%26P_500_Index

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Fad Investing Works – Until it Doesn't

Here's how the 8 richest people in the world (as estimated by Forbes Magazine) who made their money on cryptocurrency related investments fared in 2022:

Individual	Source of Wealth	Net Worth (March)	Net Worth (December)
Changpeng Zhao	Binance	$65 billion	$4.5 billion
Sam Bankman-Fried	FTX, Alameda Research	$24 billion	$0
Brian Armstrong	Coinbase	$6 billion	$1.5 billion
Gary Wang	FTX, Alameda Research	$5.9 billion	$0
Chris Larsen	Ripple, XRP	$4.3 billion	$2.1 billion
Tyler Winklevoss	Bitcoin, Gemini	$4 billion	$1.1 billion
Cameron Winklevoss	Bitcoin, Gemini	$4 billion	$1.1 billion
Barry Silbert	Digital Currency Group	$3.2 billion	$0

Imagine in a single year losing over $60 Billion USD or losing 75-100% of your wealth. Of course, that's a risk with having most of your eggs in one basket, not to mention getting caught in a bubble. We may have missed out on making a fortune when cryptocurrency was soaring, but we also missed the total collapse and bankruptcy of many cryptocurrencies and related firms. This shows that if you take a gamble on something because everyone else is, or just because it's been going up, you shouldn't be greedy. You must take profits (if you were lucky enough to make any on such a gamble) and get out of the "investment" before the bubble bursts and everyone tries to stampede out of it.

A Forbes Magazine journalist explained it this way on Dec 24, 2022. "FTX's demise was a fitting end to a year of wealth destruction in the cryptocurrency and blockchain sector. The post-pandemic economic shock, which triggered inflation and rising interest rates, sucked capital out of the speculative crypto ecosystem. Prominent firms imploded, from the $40 billion collapse in May of algorithmic stablecoin TerraUSD, to the crypto hedge fund Three Arrows (which declared for bankruptcy in July), to the bankruptcies of interest-bearing lending businesses Voyager Digital, Celsius and BlockFi. Bitcoin, the largest cryptocurrency and an industry bellwether, is down 65% from its $69,000 peak in November 2021. Meanwhile some $2 trillion of market value has fled digital assets for safer pastures. As a result, 17 of crypto's wealthiest investors and founders have collectively lost an estimated $116 billion in personal wealth since March, according to Forbes' estimates. Fifteen of them have lost more than half their fortune over the past nine months. Ten have lost their billionaire status altogether."

In traditional investing, whether lending money or buying a business, real estate, part of a business in the form of shares, a commodity like gold or any other investment, you expect to make money in the future, whether it's from a business' operating profits or rent or the appreciation of the asset's value. It makes sense not to pay more for that investment than that future profits or gains on the value of the assets are worth to you. Buying something which has no logical way to generate a profit, and which only increases in value because it's trendy, and because the price has gone up, isn't investing. It's betting on, and trying to time, the emotions of other "investors". If you bet on companies that don't have real profits or try to bet on the popularity of something increasing, you could win big – for a while. If you don't get your money out in time, you could lose it all like some crypto investors did, like dot com investors did in 2002 or tulip bulb investors did in the 1600s. It's tempting to join the crowd in owning whatever is trending, especially because of the fear of missing out on what your neighbours might be making money on. If you want to do that, remember that it's not investing, it's gambling. Never bet more than you are fully prepared to lose. With traditional dull investing, the whole market can also drop substantially, like when the economy contracts or investors are scared of a potential war or a pandemic happens. But every time that's happened in the past, the market has recovered, because investors eventually figure out that profitable businesses are worth the present value of their future profits. So price drops on solid, profitable business with good futures are rarely permanent losses. Remember Buffett's number 1 rule – don't lose money, and number 2 rule – don't forget rule , # 1. The way to do that is to buy something with tangible worth. It's boring, but it's hard, short of encountering outright fraud, to lose all of your money.

Source: These Crypto Founders And Bitcoin Moguls Lost $116 Billion In 2022 (forbes.com)
https://www.forbes.com/sites/johnhyatt/2022/12/24/these-crypto-founders-and-bitcoin-moguls-lost-116-billion-in-2022/?sh=17d173fd42b2&utm_source=newsletter&utm_medium=email&utm_campaign=dailydozen&utm_content=uaddsubscribe&cdlcid=631f620cf9c34d131019571f

In our last newsletter, there were lots of reminders about RRSP deadlines, tax slips etc. If you want to review them, all our newsletters from the last few years are available on our website, www.RoydsFinancial.com.

Let's hope 2023 is a year with minimal political or financial drama. Dull would be good for a change. No matter what happens, our fund managers will try to keep their emotions out of investing and find the best businesses they can at good prices for us to invest in. Now we just have to be patient and let them do their jobs.

Let's give the final word in this newsletter to Peter Lynch, the manager of the U.S.'s Fidelity Magellan Fund. He's famous for compound returns of over 29% for the years between 1977 and 1990, which is more than double what the main US stock index made. His record qualifies him as one of the world's greatest investors and someone we should listen to for investing advice. Here are but a few of his famous quotes and wise words. (Source: https://graciousquotes.com/peter-lynch/)

- *In the long run, it's not just how much money you make that will determine your future prosperity. It's how much of that money you put to work by saving it and investing it.*
- *People who succeed in the stock market also accept periodic losses, setbacks, and unexpected occurrences. Calamitous drops do not scare them out of the game.*
- *The trick is not to learn to trust your gut feelings, but rather to discipline yourself to ignore them. Stand by your stocks, as long as the fundamental story of the company hasn't changed.*

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